

UNITED STATES TAX COURT
WASHINGTON, DC 20217

ILLINOIS TOOL WORKS, INC. &)	
SUBSIDIARIES,)	
)	
Petitioner(s),)	
)	
v.)	Docket No. 10418-14.
)	
COMMISSIONER OF INTERNAL REVENUE,)	
)	
Respondent)	

ORDER

On August 8, 2014, petitioner filed a Motion to Strike. This motion asks the Court to strike paragraphs 3 and 7 from respondent's answer "on the ground that [r]espondent improperly asserts a substantial understatement penalty under section 6662(d)." The Internal Revenue Service (IRS or respondent) responded to this motion on September 8, 2014. This case was assigned to the undersigned on October 30, 2014. We shall deny petitioner's motion.

In a notice of deficiency dated February 11, 2014, the IRS determined a deficiency of \$70,174,594 for the 2006 taxable year. This deficiency is attributable to respondent's determination that a transfer of funds to petitioner from a foreign subsidiary constituted a taxable dividend. The notice of deficiency did not assert a penalty under section 6662(d).

Petitioner timely petitioned this Court, contending that the transfer of funds in question constituted a nontaxable return of capital. Respondent filed his answer on July 11, 2014. In paragraphs 3 and 7 of the answer, respondent alleges that, "pursuant to the provisions of I.R.C. § 6214(a), an increased amount [is] due from [p]etitioner, on the grounds that petitioner is liable for the accuracy-related penalty under I.R.C. § 6662(a) for the 2006 tax year in the amount of \$14,034,919." In moving to strike these paragraphs from the answer, petitioner notes that neither the IRS examination team nor the IRS Appeals Office proposed to assert an accuracy-related penalty with respect to the issue currently in dispute, whereas the IRS did

propose to assert this penalty with respect to another audit issue that has since been resolved.

Tax Court Rule 52 provides that the Court may order stricken from any pleading any insufficient or frivolous claim. As petitioner acknowledges, this Court does not favor motions to strike pleadings. See Evans Publ'g, Inc. v. Commissioner, 119 T.C. 242, 249 (2002) (citing Estate of Jephson v. Commissioner, 81 T.C. 999, 1001 (1983) and Allen v. Commissioner, 71 T.C. 577, 579 (1979)). A claim will not be stricken from a pleading unless it is clear that it can have no possible bearing upon the subject matter of the litigation. As we stated in Estate of Jephson, 81 T.C. at 1001:

A motion to strike should be granted only when the allegations have no possible relation to the controversy. When the court is in doubt whether under any contingency the matter may raise an issue, the motion should be denied. If the matter that is the subject of the motion involves disputed and substantial questions of law, the motion should be denied and the allegations should be determined on the merits.

Here, the assertion of the section 6662 penalty can have a possible bearing on this case; it presents a substantial question of law; and it is directly related to the controversy.

It is not uncommon for respondent to assert a penalty or an addition to tax for the first time in his answer or in an amended answer. See Pen Coal Corp. v. Commissioner, 107 T.C. 249, 257 (1996) (stating that the Court has jurisdiction when “the Commissioner determine[s] that a deficiency is attributable to fraud or negligence, after the issuance of a deficiency notice, but without requiring the Commissioner to issue a second notice of deficiency to the taxpayer”). In some cases, this may correct a prior oversight; in other cases, it may reflect new information respondent has obtained since the notice of deficiency was mailed. In either event, we have routinely permitted this.

Citing the Administrative Procedure Act (APA) and Mayo Found. for Med. Educ. & Research v. United States, 562 U.S. 44 (2011), petitioner argues that the assertion of a penalty for the first time in an answer is impermissible as a matter of law because such assertion would be inconsistent with what petitioner describes as a prior “determination” by respondent not to assert that penalty. As such, the delayed assertion of the penalty would supposedly be analogous to a disfavored “post

hoc rationalization” by the agency. See Motor Vehicle Mfrs. Ass’n v. State Farm Mut. Auto. Ins. Co., 463 U.S. 29, 50 (1983); SEC v. Chenery, 332 U.S. 194, 196 (1947).

This argument clearly proves too much. Our Rules explicitly permit respondent to assert an increased deficiency or “new matter” in his answer, Tax Court Rule 142(a), and Congress has specifically granted this Court jurisdiction to hear such claims. Section 6214(a) provides the Court with jurisdiction to redetermine a deficiency greater than that set forth in the notice of deficiency, “and to determine whether any additional amount, or any addition to the tax should be assessed, if claim therefor is asserted by the Secretary at or before the hearing or rehearing.” On petitioner’s theory, such a determination would be impermissible because it would be inconsistent with a supposed prior “determination” by respondent--embodied in the notice of deficiency--that a smaller deficiency was correct or that the new matter should not be asserted. That is clearly not the law. In this and in other respects, the specific procedures that Congress has ordained for this Court in the Internal Revenue Code may differ from the more general rules embodied in the APA.

This is not to say that respondent can delay with impunity in asserting a new matter or an increased deficiency. When respondent does so, our Rules require that the burden of proof be shifted from petitioner to respondent concerning the increased deficiency or new matter. Tax Court Rule 142(a)(1). That, rather than striking respondent’s pleading, is the “sanction” imposed by our Rules. To the extent that petitioner’s motion advances other arguments, the thrust of which is that the penalty should not be imposed, petitioner is free to advance those contentions at trial and on brief.¹

¹Petitioner contends in the alternative that the Court should order respondent “to provide a more definite statement” concerning his basis for asserting the accuracy-related penalty. Rule 36(b) provides that “the answer shall contain a clear and concise statement of every ground, together with the facts in support thereof on which the Commissioner relies and has the burden of proof.” Paragraphs 3 and 7 of respondent’s answer satisfy the requirements of Rule 36(b). We accordingly reject petitioner’s alternative request for relief.

In consideration of the foregoing, it is

ORDERED that petitioner's Motion to Strike, filed August 8, 2014, is denied.

(Signed) Albert G. Lauber
Judge

Dated: Washington, D.C.
December 2, 2014